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HADLEY'S CHAPTER ON TAXATION; A CORRECTION.

I AM much indebted to Mr. Tunell for calling my attention to an important error in the last sentence of section 500 of my *Economics*, by which, instead of saying "With a certain tax, *many* evils which exist at the outset tend to diminish as time goes on," the book says that this will be true of "*any*" evils. This is a very serious oversight, because the sentence, as it stands printed, seems to commit me unre-servedly to the Canard theory; a theory whose defects I feel strongly, and have stated quite explicitly in certain passages which Mr. Tunell has obviously overlooked or failed to understand. He says, for instance, "Professor Hadley, in his discussion of excessive taxes on one part of the community, ignores the bearing of such taxation on the community as a whole," when the passage under criticism contains the sentence, "It [such taxation] may impose an unnecessary aggregate burden on the community which will continue from year to year"—an idea which is further carried out by saying that if taxes were continuous in their operation (which they are not) "we could judge of the goodness or badness of a tax by comparing the benefits derived from its proceeds with the evils resulting from this crowding-out process. We could set ourselves to work to devise a tax system which should raise the necessary revenue with the minimum of industrial pressure." These last sentences, which contain an implied repudiation—indeed a tolerably explicit one—of those parts of Canard's theory to which Mr. Tunell takes most just exception, are omitted by him, as irrelevant, from a passage which he otherwise quotes entire.

But I will not pursue this matter further. I am under too great obligations to Mr. Tunell for what he has noted (and enabled me to correct in plate so as to prevent further misunderstanding) to take much exception to what he may perhaps have failed to note. I am too much indebted to the writers in the JOURNAL OF POLITICAL ECONOMY for the attention which they have accorded my book to weary the constituency of that JOURNAL with a quasi-personal controversy. My object is not contention, but explanation. Inasmuch as a considerable portion of the readers of the book, and a still larger proportion of the readers of the JOURNAL OF POLITICAL ECONOMY are likely to interpret the whole chapter in the light of the erroneous sentence, a brief restatement of its underlying ideas may not be out place.

It was written with a view to the explanation and possible correction

of the existing evils which make themselves felt in modern civilized countries, and most of all in the United States. These evils and dangers fall under three heads: (1) Excessive amount of taxation. (2) Taxation for the benefit of a class. (3) Defective methods of raising revenue. The first two points have been treated in previous chapters in connection with the subject of government expenditure and protection, respectively. The third remains for treatment in the chapter on government revenue. Now the practical evil under which we suffer is *uncertainty of primary incidence*. Others are as nothing in comparison with this. Any man who will look beyond the theoretical literature to the experience of assessors and the revelations of judicial inquiry can readily convince himself that this is true, and that its truth is by no means confined to the United States. This being the case, it seemed wise to give what would otherwise have been disproportionate space to the discussion of this evil; for experience shows that Adam Smith's statements on this point, though quite as explicit as my own, have failed to make their proper impression on the public mind for lack of being given sufficient prominence.

But certainty, though it is the *conditio sine qua non* of all good taxation, and the matter of practical importance to secure, cannot be made the basis of a theory of taxation; first, because, even if in process of time all *inequalities* of burden were adjusted, the question would remain whether the *aggregate* burden was brought within proper limits; second, because every change in the amount of revenue required creates a number of unadjusted burdens which must, as far as possible, be put on the shoulders of those who are able to bear them, by a system of direct taxation.

I am far from claiming that this furnishes a thoroughly satisfactory treatment of government revenue. Judged as a theory of taxation, it lacks both positiveness and definiteness. But my experience with the actual working of tax laws in America, and my observation of cases, like the Austrian sugar drawback, where we really get an insight into their working in Europe, has led me to believe that positiveness and definiteness of theory are attained at the sacrifice of truthfulness and practical efficiency. And, knowing the care which Mr. Tunell has devoted to the pursuit of economic facts, I cannot help expressing my belief that ten years hence he will look at this matter in substantially the same way that I do.

ARTHUR TWINING HADLEY.

The preceding note by Professor Hadley, seems to convey the idea that in my review I did not represent him fairly, and that my comment omitted an important modifying statement from a passage which was otherwise quoted entire. In my review I state that Professor Hadley "in his discussion of excessive taxes on one part of the community, ignores the bearing of such taxation on the community as a whole." Exception is taken to this statement, and Professor Hadley introduces the following sentences to show that he is not accurately represented: "It [such taxation] may impose an unnecessary aggregate burden on the community which will continue from year to year;" and "If taxes were continuous in their operation (which they are not) we could judge of the goodness or badness of a tax by comparing the benefits derived from its proceeds with the evils resulting from this crowding-out process," and then "We could set ourselves to work to devise a tax system which should raise the necessary revenue with the minimum of industrial pressure." These statements are regarded as abundant proof that in his discussion of excessive taxes on one part of the community he did not ignore the bearing of such taxation on the community as a whole.

Professor Hadley, I fear, did not understand the sense in which "ignore" was employed. The word was not used in the old sense—now archaic—of being ignorant of, or unacquainted with, but in the sense in which the word is now commonly used, that is, to neglect to take notice of, or to disregard. I desired to convey the idea that although recognizing that the efficiency of an industrial community was impaired by excessive taxation of some portion of it, he did not in his treatment of taxation attempt to provide against such disastrous consequences.

After showing how excessive taxes on a certain industrial group are shifted Professor Hadley says: "If all taxes were *continuous* in their operation, we might trust to this shifting process to make them equitable. We might fairly assume that in the long run the men who were able to pay the taxes would pay them, while those who were unable to pay would be crowded out of an industry. We could judge of the goodness or badness of a tax by comparing the benefits derived from its proceeds with the evils resulting from this crowding-out process. We could set ourselves to work to devise a tax system which should raise the necessary revenue with a minimum of industrial pressure. But the matter is not thus simple. Taxes are not continuous in their

operation. New grounds of expenditure arise which necessitate either an imposition of new taxes or an increase of old ones. Changes in industrial method may intensify this need by rendering the old taxes less productive; or they may operate in the reverse direction and produce a surplus which gives ground for a well-founded claim for reduction in tax rates. But whenever any tax is increased or reduced a change of economic burdens is created, which it takes time to adjust, and which may for months or years impose upon certain individuals an undue share of contributions to the public revenue, before the matter finally adjusts itself in an equitable fashion.¹

In the section just quoted, Professor Hadley considers two quite distinct things—the undue burden placed upon certain individuals and the impairment of industrial efficiency, by excessive taxation of one portion of a community. It is readily seen, however, that the section is primarily devoted to the question of equity and his treatment of the other subject is wholly in the nature of an excursion. For this reason in quoting this section, to show that Professor Hadley's treatment of the question of equity was inadequate, I left out what I considered wholly extraneous matter. With the paragraph before the reader, and with this single statement I am ready to submit the question as to whether or not the omission by me of the sentences having to do with the impairment of industrial efficiency was proper in a treatment of the subject of equity.

What is there in this section which can be adduced to show that the destruction of the industrial efficiency of a community is not disregarded? Nothing at all, so far as I can gather, except what is immediately withdrawn. In one sentence we are informed that if certain conditions existed we could devise a tax system which would raise the necessary revenue with a minimum of industrial pressure, only to be immediately informed that these conditions cannot exist. As the burden of taxation cannot by a system of experimentation and readjustment be so distributed as not to impair the industrial efficiency of the community it becomes incumbent on Professor Hadley to point out some other way. Some guiding principles should be laid down for the proper distribution of the burdens of taxation when taxes are imposed but none are given. The few adventitious remarks to which attention has been directed, constitute the whole of his treatment of this important subject.

¹ HADLEY, *Economics*, p. 459.

In order to obtain certain positive results, it appeared to me that Professor Hadley was too ready to look great evils squarely in the face, and meet any objection to their further continuance with the contention that any attempt to remedy these evils might result in the introduction of still others. He says, for instance, "In the assessment of corporate property, as in the case of real estate, no deduction should be allowed for indebtedness. If the attempt is made to tax the debt in the hands of the holders, it will fail. The tax should reach the whole property of the corporation without reference to the question of its ownership."¹ And again he says, "Apart from the possibility of progressive or compensatory taxation, the theoretical advantages and disadvantages of income and property taxes are so closely balanced that the question between them must be decided on the basis of certainty of assessment and ease of collection. In the former respect the property tax has, perhaps, a slight advantage. The measurement of capital presents fewer theoretical difficulties than the measurement of income; for we have to make a number of uncertain deductions in the latter case which are not involved in the former."² As it is not to be presumed that Professor Hadley is unaware that there is a very numerous class of men who enjoy large incomes, yet own but little property, it must be inferred that he is willing to let these men escape taxation rather than make some sacrifice of certainty. To secure simplicity in his tax system he seems to be ready to make any sacrifice. In this respect he places himself in opposition to most of the great authorities on taxation, who hold that the simplicity that once obtained must be given up, before a tax system can be framed which will tap the numerous new sources of income resulting from the new industrial order.

Professor Hadley objects to being regarded as an advocate of the diffusion theory of taxation; his book, however, places him in this category. This we are now informed contains a serious error. The book states that "with a certain tax *any* evils which exist at the outset tend to diminish as time goes on."³ It should read "with a certain tax *many* evils which exist at the outset tend to diminish as time goes on." Without the correction which Professor Hadley has now made his statement would commit him to the diffusion theory. That the chapter is confusing because of the error Professor Hadley seems to admit, for he says: "Inasmuch as a considerable portion of the readers of the book, and a still larger proportion of the readers of

¹ P. 454.

² P. 464.

³ P. 452.

the JOURNAL OF POLITICAL ECONOMY are likely to interpret the whole chapter in the light of the erroneous sentence, a brief restatement of its underlying ideas may not be out of place."

This restatement still leaves matters in a rather unsatisfactory condition. If "with a certain tax *many* [but not *any*] evils tend to diminish as times goes on," it would be interesting to know a little more definitely than we are told just what evils would tend to diminish. "*Uncertainty of primary incidence*" is not such a familiar term that it can be left with the scant explanation which is given to it.

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